BEFORE THE

PUBLIC UTILITIES COMMISSION
OF THE
STATE OF RHODE ISLAND
AND PROVIDENCE PLANTATIONS

IN THE MATTER OF

The Application of New England	**)**	
Gas Company for an Increase	**)**	**Docket No. 3436**
In its Gas Cost Recovery Charge	**)**	

DIRECT TESTIMONY OF WITNESS
BRUCE R. OLIVER

On Behalf of

The Division of Public Utilities

OCTOBER 16, 2003

TESTIMONY OF BRUCE R. OLIVER
Docket No. 3436
October 16, 2003

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS FOR THE RECORD.

A. My name is Bruce R. Oliver. My business address is 7103 Laketree Drive, Fairfax Station, Virginia, 22039.

Q. BY WHOM AND IN WHAT CAPACITY ARE YOU EMPLOYED?

A. I am employed by Revilo Hill Associates, Inc., and serve as President of the firm. I manage the firm's business and consulting activities, and I direct its preparation and presentation of economic, utility planning, and policy analyses for our clients.

Q. ON WHOSE BEHALF DO YOU APPEAR IN THIS PROCEEDING?

A. My testimony in this proceeding is presented on behalf of the Division of Public Utilities (hereinafter "the Division").

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS PROCEEDING?

A. This testimony addresses issues relating to the September 2, 2003 Annual Gas Cost Recovery (GCR) filing of New England Gas Company (hereinafter “NEG” or “the Company”).

Q. IS NEG PROPOSING TO INCREASE ITS GCR CHARGES?

A. Yes. The Company proposes to increase its GCR charges for all firm sales service rate classifications. The Company also proposes to adjust its charges for marketer transportation services and increase its charges for Natural Gas Vehicle Service.

Q. HOW LARGE ARE THE INCREASES IN GCR CHARGES THAT NEG PROPOSES?

A. NEG's proposed increases vary by rate classification. The magnitude of those increases also will depend upon how much of the Company's Deferred Gas Cost Balance is recovered through its proposed charges. The testimony of NEG witness Michael J. Harn presents rates with full recovery of its Deferred Gas Cost Balance. He also offers a discussion of the possibility of implementing new GCR rates that provide for less than full recovery of the Company's Deferred Gas Cost Balance to mitigate increases in customers' bills.

Witness Harn presents an analysis of bill impacts resulting from the Company's computed GCR charges with <u>full recovery</u> of its deferred gas cost balance in Attachment MJH-3. That analysis, which computes percentage increases in "Typical Sales Service Bills" for each of NEG's firm sales service rate classifications, depicts total bill increases ranging from a low of **4.7%** for former ProvGas Residential Non-Heating customers to a high of **12.7%** of Large C&I High Load Factor customers.

Attachment MJH-4 provides a summary of the results of a similar analysis of total bill impacts with GCR charges structured to recover only 50% of the Company's deferred gas cost balance. This alternative analysis shows bill increases ranging from a low of **2.6%** for Residential Non-Heating customers in the former Providence Gas Company (ProvGas) service territory to a high of **8.1%** for former ProvGas Large C&I High Load Factor customers.

Q. DO YOU HAVE ANY CONCERNS REGARDING THE BILL IMPACT ANALYSES THAT THE COMPANY HAS PRESENTED TO DATE IN THIS PROCEEDING?

A. Yes, I do. As discussed at pages 20-21 of my recently filed testimony in the Company's pending Distribution Adjustment Charge (DAC) proceeding, the "typical " sales service bill impacts that the Company computes are based on usage levels that for several rate classes depart significantly from forecasted average gas annual use for those classes.[1] As a result, those filed bill impact analyses are not necessarily descriptive of the rate impacts that most, or even a majority, of customers within certain rate classes will experience. Moreover, the Company provides no indication of the extent of variation among the bill impacts for customers of varying levels of use within each rate class. In proceedings such as this, where important policy decisions may be influenced by bill impact considerations, greater information regarding the distributions of numbers of customers and bill impact percentages by annual usage level within each rate class is of key importance to the Commission's decision-making process.

In addition, I submit that while analyses of total bill impacts have value, the Commission also needs greater perspective regarding the magnitude of the gas cost increases that the Company seeks, that cannot be easily observed from NEG's filed bill impact analyses. For example, the table below summarizes the increases in NEG's GCR charges that would result if those charges are designed to provide for full recovery of the Company's deferred gas cost balance.

Computed Increases in GCR Charges by Rate Classification

Rate Classification	Current GCR Rate ($/Therm)	Proposed GCR Rate ($/Therm)	Increase $ ($/Therm)	Increase %
Residential				
Non-Heating	$0.7120	$0.8195	$0.1075	15.10%
Heating	$0.7120	$0.8195	$0.1075	15.10%
Commercial & Industrial				
Small	$0.7120	$0.8195	$0.1075	15.10%
Medium	$0.6988	$0.8099	$0.1111	15.90%
Large Low Load Factor	$0.7069	$0.8113	$0.1044	14.77%
Large High Load Factor	$0.6604	$0.7852	$0.1248	18.89%
Extra Large Low Load Factor	$0.6948	$0.8205	$0.1257	18.09%
Extra Large High Load Factor	$0.6239	$0.7751	$0.1512	24.24%

1 See Exhibit BRO-2 attached to the October 7, 2003 testimony of Bruce R. Oliver in Docket No. 3548.

Thus, the increases in the GCR component of the Company's rates (assuming full recovery of the Company's deferred gas cost balance), range from roughly 15% to 24%. Moreover, the majority of the computed increases are associated with recovery of NEG's end-of-year deferred gas cost balance. Recovery of that deferred balance represents a cost of about **$0.07 per therm** on average for all firm sales service customers. For Residential and Small Commercial customers, that $0.07 per therm equates to more than **65%** of the total increase in GCR charges that is necessary for full recovery of the Company's end-of-year deferred gas cost balance.

Q. SHOULD THE COMMISSION ADOPT NEG'S PROPOSAL TO DEFER RECOVERY OF DEFERRED GAS COSTS IN EXCESS OF 5% OF PROJECTED GAS COSTS FOR THE GCR PERIOD?

A. The question regarding the portion of the Company's deferred gas cost balance that should be recovered through the revised GCR charges is a matter of policy over which the Commission may exercise considerable discretion. However, I recommend that the Commission attempt to minimize the portion of the Company's deferred gas cost balance that it defers for recovery in future GCR periods. Although I support reasonable and appropriate efforts to moderate the impacts of changes in the Company's GCR charges on customers' bills, such deferrals may not be well advised in this proceeding.

Q. WHAT FACTORS OTHER THAN BILL IMPACTS SHOULD THE COMMISSION CONSIDER WHEN ASSESSING WHETHER RECOVERY OF A PORTION OF THE COMPANY'S CURRENT DEFERRED GAS COST BALANCE SHOULD BE POSTPONED?

A. I have identified at least four factors, other than bill impacts, that warrant consideration. Those factors include:

- Projections of future gas costs
- Anticipated future DAC levels
- Weather
- Interest Rates

Q. WHAT INFLUENCE SHOULD PROJECTIONS OF FUTURE GAS COSTS HAVE ON DECISIONS REGARDING THE POSTPONEMENT OF RECOVERY OF DEFERRED GAS COST BALANCES?

A. Any decision to defer gas cost recoveries to future periods must consider the gas cost levels upon which such future recovery of deferred gas cost balances will be superimposed. In a market characterized by expectations of declining prices for natural gas, decisions to postpone recovery of deferred gas cost balances for recovery in future periods may help to moderate year-to-year fluctuations in GCR rates. However, in the present market most analysts still perceive considerable upward pressure on natural gas prices in periods beyond the coming winter. Moreover, that upward pressure on natural gas prices may intensify with improvements in the health of the nation's economy, since economic growth generally is associated with increased energy demand, and natural gas is being relied upon to fuel an increasing share of our national energy demand growth requirements. Although the Commission can continue to expect considerable volatility in natural gas prices, it should also expect natural gas prices will continue trending upward. In that context, any gas cost recovery that is postponed to future gas supply periods will most likely be added to gas prices that are above the levels that NEG projects on average for the coming year.

Q. HOW SHOULD EXPECTATIONS REGARDING FUTURE DAC RATES ENTER INTO THE COMMISSION'S CONSIDERATIONS REGARDING THE POSTPONEMENT OF RECOVERY OF DEFERRED GAS COST BALANCES?

A. When overall impacts on customers' bills are considered, changes in GCR rates must be assessed in the context of anticipated changes in DAC charges.

Q. HOW SHOULD WEATHER CONSIDERATIONS ENTER INTO COMMISSION DECISIONS REGARDING THE POSSIBLE POSTPONEMENT OF RECOVERY OF DEFERRED GAS COST BALANCES?

A. The bill impact analyses that NEG presents are presumed to reflect normal weather. Those analyses also implicitly assume that customers' gas use requirements do not change from year-to-year. But, the bills customers paid last year were the product of substantially colder than normal weather. Although temperatures and heating degree day requirements for future periods cannot be forecasted with a high degree of confidence, it can be concluded that the likelihood that heating degree day totals for the coming winter will equal or exceed those for last winter is comparatively small. Thus, a high probability exists that NEG customers will consume less gas in the coming year than they did last year, and such reduced levels of gas consumption will tend to lower customers' bills relative to their levels in the prior year.[2]

Q. IN WHAT MANNER SHOULD INTEREST RATE CONSIDERATIONS IMPACT GAS DECISIONS REGARDING POSSIBLE POSTPONEMENT OF GAS COST BALANCES?

[2] If the prior year had been warmer than normal, expectations would favor increased natural gas consumption and increased total bills for consumers.

A. At present short-term interest rates (i.e., the rates that NEG can be expected to incur to carry deferred gas cost balances) are quite low. As a result, the added interest costs that the Company, and eventually ratepayers, would incur by postponing recovery of a portion of NEG's current deferred gas cost balance for another year may be comparatively small. However, many financial forecasters foresee an upward trend in interest rates over the next year. Higher interest rates will serve to increase the costs of carrying deferred gas cost balances. In addition, all other things being equal, higher interest rates will increase the working capital component of NEG's GCR calculations for the next GCR period. Thus, a decision to postpone recovery of a portion of the Company's current deferred gas cost balance may not add substantially to NEG's GCR costs, but it may amplify the amount of increase that can be expected in GCR rates for the next GCR period.

Q. DO YOU SUPPORT THE COMPANY'S PROPOSAL TO ESTABLISH A POLICY THAT GCR FACTORS SHOULD BE DESIGNED TO RECOVER ONLY THAT PORTION OF THE DEFERRAL BALANCE THAT EXCEEDS 5% OF PROJECTED GAS COSTS FOR THE UP-COMING GCR PERIOD?

A. No, I do not. I submit that such determinations are more appropriately made on a case-by-case basis with each of the factors discussed properly weighted to reflect the best information available at the time.

Q. ARE THE GCR CHARGES THAT NEG WITNESS HARN PRESENTS IN ATTACHMENT MJH-1 PROPERLY COMPUTED?

A. Yes. My review of Mr. Harn's testimony and supporting attachments finds that, in general, the Company's GCR calculations follow established procedures and are mathematically accurate. Questions arise, however, with respect to the manner in which gas cost reconciliation balances have been allocated among rate classes.

Q. HOW HAS NEG APPROACHED THE ALLOCATION OF RESPONSIBILITY FOR DEFERRED GAS COST BALANCES AMONG RATE CLASSES?

A. NEG's efforts to allocate its gas cost reconciliation balance among rate classifications are detailed in Attachment MJH-2 to the September 2, 2003 testimony of witness Harn. Under the procedures that the Company employed, reconciled balances for the entirety of the Company's firm service gas supply obligations are computed for the 12 months ended June 30, 2003 for each of five gas cost categories (or "buckets"). Those gas cost categories include:

- Fixed Gas Supply Costs,
- Variable Gas Supply Costs,
- Storage Fixed Costs,

- Storage Variable Product Costs, and
- Storage Variable Non-Product Costs.

Class responsibilities for the reconciled balance of gas costs for each of those five gas cost categories are then allocated to rate classifications. The allocation factors applied vary by cost category. Reconciled balances for Supply Fixed Costs and Storage Fixed Costs are allocated to classes on the basis of design winter sales. Supply Variable Costs and Storage Variable Costs are divided into "locked" and "unlocked" categories. Locked Variable Costs are allocated to classes on the basis of forecasted sales. Allocations of Unlocked Variable Costs to rate classes are accomplished using sales in excess of forecasted levels for each rate class.

Q. ARE THE COMPANY'S ALLOCATIONS OF GAS COST RECONCILIATION BALANCES FOR THE 12 MONTHS ENDED JUNE 30, 2003 REASONABLE?

A. Recognizing that this was the first time the Company engaged in an effort to differentiate the allocation of reconciled balances by rate class, I find that the Company's efforts to allocate gas cost reconciliation balances for the 12 months ended June 30, 2003 are generally reasonable. I particularly appreciate the Company's efforts to differentiate its allocations of reconciled balances for locked and unlocked components of its variable costs. Although some further refinement the Company's allocation procedures may be warranted, the Division intends to continue its dialogue with the Company on this matter in an attempt to resolve conceptual differences while keeping the magnitude of the reconciliation task within reasonable bounds.

A particular concern of mine regarding the Company's analysis for the 12 months ended June 30, 2003 is that FT-1 customers who returned to sales service were not charged with responsibility for any of the Company's Fixed Storage Costs. This is a problem that has been addressed on a going-forward basis through the recently approved Transitional Sales Service Tariff. However, it is not adequately addressed in NEG's allocations of reconciliation balances for the 12 months ended June 30, 2003. As a result, I believe the cost responsibilities of FT-1 customers for that past period are understated. This shortcoming does not appear to have a dramatic affect on the costs allocated to other classes of firm sales service customers, but its impact on FT-1 customers could be noticeable.

Q. DO YOU SUPPORT THE COMPANY'S PROPOSED INCREASE IN ITS CHARGES FOR NATURAL GAS VEHICLE SERVICE?

A. I find that an increase in the Company's commodity charge for Natural Gas Vehicle (NGV) service is appropriate. However, it appears that the proposed charge of

$0.5639 is slightly understated. The appropriate charge should be the Supply Variable Cost Factor from Attachment MJH-1, page 1, line 3, of $5.6838 per Dth times the Uncollectible percentage (2.10%) and divided by 10 to convert the resulting rate to a per therm charge. Thus, the proposed commodity charge for NGV service should be $0.5803 per therm.

Q. WHAT ADJUSTMENT TO MARKETER TRANSPORTATION CHARGES DOES NEG SEEK IN THIS PROCEEDING?

A. NEG proposes changes in its Marketer Transportation charges for (a) the FT-2 Storage Service Charge, (b) the Pool Balancing Charge, and (c) the weighted average Upstream Pipeline Transportation Cost. The FT-2 Storage Service Charge is reduced from $0.0439 per therm of throughput to $0.0421 per therm. On the other hand the Company's proposed charges for Pool Balancing and Upstream Pipeline Capacity are increased. NEG proposed to increase its Pool Balance Charge from $0.0015 to $0.0021 per % of elected per therm throughput. The Company computes an increase in its base charge for Upstream Pipeline Capacity from $0.0885 to $0.1003 per therm of capacity.

Q. ARE THE CHANGES IN MARKETER TRANSPORTATION CHARGES THAT THE COMPANY PROPOSES REASONABLE AND APPROPRIATE?

A. Yes. The Company's calculations for those charges appear consistent with its past practices, and should be approved.

Q. IS THE BTU CONVERSION FACTOR THAT NEG PROPOSES FOR THE COMING WINTER PERIOD REASONABLE?

A. Yes. The 1.029 conversion factor that NEG computes appears to accurately portray the Company's experience on average from last winter. Although there were some noticeable fluctuations in the Btu's per Mcf that NEG reported on a daily basis for last winter, those fluctuations generally fell within a range of plus or minus .015 from the computed 1.029 average for the winter period. Furthermore, daily factors that approached the extremes of that range were typically short-lived, and do not appear to yield substantial month-to-month changes in NEG's average Btu's per Mcf. Moreover, despite the extreme weather conditions during the period over which the 1.029 conversion factor was computed, the difference between that factor and the currently applicable summer season conversion factor (i.e., 1.026) is also quite small. Thus, the experience to date appears to portray little, if any, need for monthly varying Btu conversion factors and even raises questions regarding the need for seasonally differentiated conversion factors.

Q. SHOULD THE COMMISSION APPROVE THE MISCELLANEOUS TARIFF CHANGES FOR WHICH NEG SEEKS APPROVAL IN THIS PROCEEDING?

A. Yes. The Company has proposed tariff language changes to incorporate provisions necessary for the implementation of the Asset Management and Gas Procurement incentives that this Commission approved in Order No. 17444.

Q. HAVE YOU REVIEWED THE DETAIL OF THE GAS COST PROJECTIONS THAT THE COMPANY PROVIDES THROUGH THE TESTIMONY OF WITNESS GARY BELAND?

A. Yes, I have.

Q. ARE THE COMPANY'S GAS COST PROJECTIONS REASONABLE?

A. Yes. Understanding that commodity prices for gas purchases that have not been locked may be subject to considerable volatility, the gas cost projections that NEG presents offer a reasonable assessment of the Company's projected gas costs for the coming GCR period.

Q. HAS NEG REASONABLY AND APPROPRIATELY DETERMINED ITS PATH-SPECIFIC SURCHARGES/CREDITS FOR CAPACITY ASSIGNED TO GAS MARKETERS?

A. Yes, it has. Attachment GLB-3 to the witness Beland's September 2, 2003 testimony presents detailed support for the Company's proposed surcharges and credits for specific pipeline paths that are developed in accordance with previously accepted procedures and appear to be accurately computed.

Q. HAVE YOU REVIEWED THE PORTION OF WITNESS BELAND'S SEPTEMBER 2, 2003 TESTIMONY AT PAGES 11 AND 12 IN WHICH HE DISCUSSES CHANGES TO NEG'S GAS SUPPLY PORTFOLIO IN THE FORM OF CHANGES AND ADDITIONS TO ITS PIPELINE CAPACITY AND LONG-TERM GAS SUPPLY COMMITMENTS.

A. I have. I have also reviewed analyses of the Company's projected gas supply requirements under design conditions for the coming winter that were provided in response to informal requests made of the Company.

Q. HAS NEG ADEQUATELY DEMONSTRATED THAT THE CHANGES AND ADDITIONS MADE TO ITS GAS SUPPLY PORTFOLIO REASONABLY SERVE TO MINIMIZE ITS COSTS OF GAS AND PROVIDE AN APPROPRIATE LEVEL OF FIXED COSTS FROM WHICH TO MEASURE FIXED COST SAVINGS AND COMPUTE ASSET MANAGEMENT INCENTIVES?

A. The Company's filed September 2, 2003 testimony and exhibits in this proceeding do not explicitly address the reasonableness of its projected fixed gas supply costs. Through informal discovery, however, the Company provided a multi-page spreadsheet which details the relationships between its supply capabilities and its forecasted design winter and design day requirements. Mr. Beland and Mr. Czekanski also took considerable time to walk me through that analysis and answer numerous questions regarding its content and implications. On the basis of my review of the additional analysis NEG has provided, I find that under design conditions the Company's gas supply and storage resources are heavily utilized, leaving little unused gas supply capability.[3] This leaves the potential that the Company would have excess supply capabilities under non-design conditions that could generate fixed cost savings through capacity release activities. However, that potential is addressed through the Company's forecasted capacity release credits, which appear to be reasonably in-line with its actual levels of capacity release revenue in recent years. Thus, I find little basis for questioning the reasonableness of NEG's fixed gas supply and fixed storage costs.

[3] It should be noted that NEG's design day and design winter analyses assume that incremental use per degree day in peak winter months is greater than average use per degree day for the winter season. This is an assumption not used in similar prior analyses. That assumption is also not consistent with assumptions regarding the relationship between incremental degree days and incremental gas use that have been relied upon for ratemaking purposes. If gas use per degree day were assumed to be uniform throughout the winter, the Company's projected fixed costs for Supply and Storage may not be fully justifiable. However, the rationales and analytic explanations offered for the Company's assumptions in this proceeding do appear reasonable.

In the future, however, NEG should be required to explicitly address the reasonableness of its projected fixed gas supply and storage costs as part of its direct presentation in annual GCR filings.

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes, it does.